

***United States Court of Appeals
for the Second Circuit***



**APPELLANT'S
BRIEF**

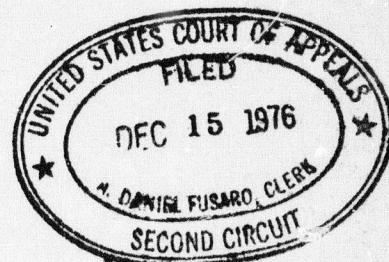
76-5040

ORIGINAL

Docket No. 76 - 5040

(76 B 2341)

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT



IN THE MATTER OF

23 E. 74 REALTY CORP.,

Debtor-Appellant.

B
p/s

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

DEBTOR-APPELLANT'S BRIEF

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

-----X
IN RE

23 E. 74th REALTY CORP.,

Case No: 76-5040

Debtor-Appellant.
-----X

PRELIMINARY STATEMENT

On October 19, 1976, the debtor-appellant filed a voluntary petition under Chapter X, which petition was referred to the Hon. Richard Owen for approval or disapproval. Simultaneously with the filing of the petition, the debtor-appellant filed an ex-parte application pursuant to Chapter X, §113, of the Bankruptcy Act, to stay a sale of its sole asset pursuant to a judgment of foreclosure entered in the Supreme Court, New York County. Judge Owen referred the application for a temporary stay prior to approval action on debtor's petition to the Hon. Lee P. Gagliardi for disposition. On October 20, 1976, at 9:00 A.M. after a hearing held at 4:30-5:00 P.M. on October 19, 1976, Judge Gagliardi not only denied the stay requested pursuant to Chapter X, §113 of the Act, but also vacated the automatic stay mandated by Bankruptcy Rule 10-601.

This is an appeal from said denial of the temporary stay and from the vacating of the automatic stay mandated by Rule 10-601

of the Bankruptcy Rules.

ISSUES PRESENTED FOR REVIEW

1. Did the lower Court have the authority to deny the application for a stay pursuant to Chapter X, §113 of the Bankruptcy Act in light of Rule 10-601 of the Bankruptcy Rules which provides that the filing of a petition operates as an automatic stay of all proceedings to enforce liens against real property?

2. If the lower Court had such authority, did the Court abuse its authority by failing to grant a temporary stay pending the approval or disapproval of the petition for relief under Chapter X?

3. Did Judge Gagliardi, prior to the decision of Judge Owen to approve or disapprove the petition under Chapter X, have the authority to vacate the automatic stay pursuant to Rule 10-601 without a plenary hearing on the issue of good faith?

The debtor-appellant contends that Judge Gagliardi was in error in refusing to execute the order granting a stay pursuant to Chapter X, §113 of the Act; and was further in error in vacating the automatic stay provided by Rule 10-601, and Rule 601 of the Bankruptcy Rules.

NATURE OF THE CASE

On October 19, 1976, the debtor-appellant petitioned the United States District Court for the Southern District of New York under Chapter X of the Bankruptcy Act (Rule 10-104 Bankruptcy Rules) for a corporate reorganization under said Act.

The petition was filed, fee paid and referred to Judge Owen to approve or disapprove the petition.

On November 24, 1976, Judge Owen referred the petition to Bankruptcy Judge Edward J. Ryan for a hearing on the approval or disapproval of said petition. The hearing as of yet has not been held.

Simultaneously with the filing of the petition, debtor-appellant filed an application for a temporary stay pending approval pursuant to Chapter X, §113 of the Bankruptcy Act to stay a foreclosure sale in an action commenced by Amfac Mortgage Corporation to be held pursuant to an order and judgment of foreclosure and sale duly made and entered in the Supreme Court, New York County, on July 21, 1976, mandating that said sale be held on October 20, 1976.

Judge Gagliardi, to whom the matter was referred by Judge Owen, had the attorneys for Amfac Mortgage Corporation, Shea, Gould, Climenko, Kramer & Casey, appear at his courtroom at

approximately 4:30 on October 19, 1976 for a hearing on said application.

The following morning at 9:00 A.M., he rendered a decision not only denying the application for a temporary stay of the foreclosure sale on October 20, 1976, but vacating the automatic stay provided by Rule 601 of the Bankruptcy Rules which are further promulgated by Rule 10-601 of the said Bankruptcy Rules.

RELEVANT FACTS

23 E. 74 Realty Corp. is a New York corporation which owns and operates real property known as 23 East 74th Street, New York, New York. Said property consists of a sixteen story, multiple dwelling containing 83 apartments and commercial establishments operating under the trade name "Volney Hotel."

In 1974, the debtor borrowed from Amfac Mortgage Corporation as part of an acquisition and construction loan, \$2,500,000.00 which was secured by a first mortgage on said real property. In addition thereto, the debtor borrowed another \$350,000.00 from other sources.

The first mortgage was due on September 11, 1975 and was not paid and an action in foreclosure commenced. On July 21, 1976 a judgment of foreclosure and sale was entered in the Supreme Court, New York County, which provided for the sale to take place on October 20, 1976 at 10:00 A.M. The judgment was for the amount of \$2,919,687.49, plus interest, costs, allowances, etc. From the exhibits annexed in the moving papers, it appeared the building was now almost fully rented with an approximate annual gross rental of \$600,000.00, with net sum available prior to the payment of debt services and interest of \$325,000.00. (A 18 and 19) The payment of all expenses was under the joint control of Amfac Mortgage

Corporation and the debtor. The officers of the debtor were not taking salaries. The debtor had pending application for an FHA mortgage commitment in the amount of \$2,850,000.00 for which the FHA had received a commitment fee of \$6,000.00 and there was a mortgage application pending with the Kosta Group for \$3,200,000.00. The debtor alleged in its petition that the approval of either one of these applications would pay the indebtedness due the first mortgage, save the equity of the debtor in the property and provide for full payment of all unsecured creditors.

APPLICABLE STATUTES

CHAPTER X, §113

PRIOR TO THE APPROVAL OF A PETITION, THE JUDGE MAY UPON CAUSE SHOWN GRANT A TEMPORARY STAY, UNTIL THE PETITION IS APPROVED OR DISMISSED, OF A PRIOR PENDING BANKRUPTCY, MORTGAGE FORECLOSURE OR EQUITY RECEIVERSHIP PROCEEDING AND OF ANY ACT OR OTHER PROCEEDING TO ENFORCE A LIEN AGAINST A DEBTOR'S PROPERTY, AND MAY UPON CAUSE SHOWN ENJOIN OR STAY UNTIL THE PETITION IS APPROVED OR DISMISSED THE COMMENCEMENT OR CONTINUATION OF A SUIT AGAINST A DEBTOR. (11 USC 513). July 1, 1898, as added June 22, 1938, c. 575, §1, 52 Stat. 884.

RULE 10-601

Petition as Automatic Stay of Actions Against Debtor and Lien Enforcement

(a) Stay of Actions and Lien Enforcement. A petition filed under Rule 10-104 or 10-105 shall operate as a stay of the commencement or the continuation of any court or other proceeding against the debtor, or the enforcement of any judgment against it, or of any act or the commencement or continuation of any court proceeding to enforce any lien against its property, or of any court proceeding for the purpose of the rehabilitation of the debtor or the liquidation of its estate.

(b) **Duration of Stay.** Except as it may be terminated, annulled, modified, or conditioned by the bankruptcy court under subdivision (c), (d), or (e) of this rule, the stay shall continue until the case is closed, dismissed or converted to bankruptcy or the property subject to the lien is, with the approval of the court, abandoned or transferred.

(c) **Relief from Stay.** On the filing of a complaint seeking relief from a stay provided by this rule, the bankruptcy court shall, subject to the provisions of subdivision (d) of this rule, set the trial for the earliest possible date, and it shall take precedence over all matters except older matters of the same character. The court may, for cause shown, terminate, annul, modify, or condition such stay. A party seeking continuation of a stay against lien enforcement shall show that he is entitled thereto.

(d) **Ex Parte Relief from Stay.** On the filing of a complaint seeking relief from a stay against any act or proceeding to enforce a lien or any proceeding commenced for the purpose of rehabilitation of the debtor or the liquidation of its estate, relief may be granted without written or oral notice to the adverse party if (1) it clearly appears from specific facts shown by affidavit or by a verified complaint that immediate and irreparable injury, loss, or damage will result to the plaintiff before the adverse party or attorney can be heard in opposition, and (2) the plaintiff's attorney certifies to the court in writing the efforts, if any, which have been made to give the notice and the reasons supporting his claim that notice should not be required. The party obtaining relief under the subdivision shall give written or oral notice thereof as soon as possible to the debtor, the trustee, receiver, or debtor in possession or, if none has been designated or qualified, to the petitioner or petitioners and, in any event, shall forthwith mail to such person or persons a copy of the order granting relief. On 2 days' notice to the party who obtained relief from a stay provided by this rule without notice or on such shorter notice to that party as the court may prescribe, the adverse party may appear and move its reinstatement, and in that event the court shall proceed to hear and determine such motion as expeditiously as the ends of justice require.

(e) **Availability of Other Relief.** Nothing in this rule precludes the issuance of, or relief from, any stay, restraining or injunction order when otherwise authorized.

PAGE 10 APPEARS

TO BE MISSING.

POINT I

THE DISTRICT COURT HAD NO AUTHORITY TO
REFUSE TO SIGN THE PROFERED ORDER

Whereas, prior to 1973, the granting of a stay pursuant to Chapter X, §113, of the Bankruptcy Act was discretionary, it is clear that as of April 24, 1973, when the United States Supreme Court ordered the Bankruptcy Rules into effect as of October 1, 1973, pursuant to §2075, Title 28, it no longer had such discretion. Not only did the United States Supreme Court enunciate the policy of the Courts under its jurisdiction with regard to the administration of the judiciary of the Bankruptcy Act, it mandated the policy of the Federal Courts with regard to, among other things, the granting of stays in bankruptcy proceedings.

It is clear that without the enactment of the Bankruptcy Rules in 1973, that until the petition under Chapter X was approved by the District Judge (§148 of the Act, 11 USC 548), the mere filing of a bankruptcy proceeding under Chapter X of the Act did not ipso facto act as a stay of a mortgage foreclosure proceeding. That under the Act, application had to be made pursuant to Chapter X-113 (11 USC 513) for a temporary stay of any proceeding to enforce a lien against a debtor's property until the petition was acted upon. In Re Long Island Properties, D.C.N.Y. 1941, 42 F. Supp. 323.

Rule 601 and Rule 10-601 of the Bankruptcy Rules provided that the mere filing of a petition under Rule 10-104 operates as a stay of any Court proceeding to enforce a lien against the property of a debtor or the liquidation of his estate.

Thus, the matter of discretion inherent in the District Court's judicial power as to the granting of the stay in general was proscribed by the enactment of the Bankruptcy Rules.

Chapter X-113 of the Act was last amended June 22, 1938; Rule 601 was promulgated and effective October 1, 1973, thus it is clear the District Court no longer had discretion but was obligated to execute the ex-parte order presented by the debtor.

POINT II

THE DISTRICT COURT ABUSED ITS DISCRETION IN DENYING THE APPLICATION FOR A TEMPORARY STAY

Even if the Court's inherent discretionary power could be exercised notwithstanding the promulgation of the Bankruptcy Rules, the Court abused said discretion.

Whether to enter a stay depends largely on the unique facts of the particular case before the Court. In Re J.S. Gissel & Co., D.C. Tex. 1965, 238 F. Supp. 130. It is clear that the District

Court, in the reorganization proceeding, is empowered to enter an order staying the sale of a mortgaged property under foreclosure decree obtained in a state Court. Mongiello Bros. Coal Corp. v. Houghtaling Properties, Inc., C.A. Fla. 1962, 309 F.2d 925.

It is unfortunate, but understandable that the debtor did not file a Chapter X petition until the eve of the foreclosure sale. From the moving papers which were the only papers before the Court, it appeared that the debtor had two mortgage applications pending, with the Federal Housing Authority and the Kosta Group. The granting of either mortgage would have repaid the mortgage being foreclosed and provide sufficient funds to pay the unsecured credits of the debtor. The debtor being in financial difficulty, did not want to expend funds required to retain counsel to commence a Chapter X proceeding where the monies could be better spent paying the closing costs incurred in closing a new permanent mortgage. Although the attorneys for Amfac Mortgage Corporation (Amfac), the plaintiff in the foreclosure proceeding, appeared in Court and orally alleged lack of good faith by the debtor, there were no evidentiary facts presented to the District Court to sustain that position nor were there any evidentiary facts to refute the allegations contained in the petition that there was an application pending before the Federal Housing Authority for a permanent mortgage and there was also a similar application pending before

a private mortgage funding group.

There was no evidence presented that the mere stay of the sale for several days pending the approval or disapproval of the petition would cause the mortgagee to incur additional expense or diminish the amount to be realized by the lien creditor should the mortgage sale be held at a later date. To the contrary, the evidence before the Court was that the current obligations were being paid and that all monies being received were expended over the joint signature of the debtor and Amfac.

The debtor-appellant had an absolute right to file for relief under Chapter X. In Re Terrace Lawns Memorial Gardens, C.A. Idaho 1958, 256 F.2d 398. A period of time was required until the District Court could complete its investigation and a plan for reorganization presented. Without a stay, the purposes of the Bankruptcy Act would be frustrated and the ability of the District Court to effectuate a reorganization would be frustrated or nullified. See In Re Terrace Lawns Memorial Gardens, supra, In Re Delta Food Processing Corp., C.A. Miss. 1971, 446 F.2d 437. The refusal to grant a stay pursuant to Chapter X-113 of the Act denied the debtor-appellant its right of a hearing on the issue of good faith and approval of its petition under Chapter X of the Act. Thus, the decision of Judge Gagliardi represents an abuse of discretion.

POINT III

THE DISTRICT COURT HAD NO AUTHORITY TO
VACATE THE STAY PROVIDED IN RULE 10-601
WITHOUT COMPLIANCE WITH SAID RULE

The question of approval of the petition for relief under Chapter X of the Act having been assigned to the Hon. Richard Owen, D.J., Judge Gagliardi had no authority to vacate the automatic stay provided by Rule 601 of the Bankruptcy Rules.

As set forth above, any corporation has an inherent right to seek relief under Chapter X of the Act. In Re Terrace Lawns Memorial Gardens, supra.

Under the Act assuming compliance with §130 of the Act (11 USC 530) thereof, the Court is mandated by §141 of the Act (11 USC 541) to enter an order approving the petition if satisfied it has been filed in good faith or dismissing the petition if it is not so satisfied. The approval of the petition acts as an automatic stay of all mortgage foreclosure proceedings. (§148 of the Act, 11 USC 548.) The Act defines the words "good faith" (11 USC 546). In this context, the question before the District Court is whether it is unreasonable to expect that a plan of re-organization can be effected. (§146 Bankruptcy Act, 11 USC 546(3)). In determining good faith, the Court can determine the same from the face of the petition or as a result of a hearing in which evidence

can be presented on said issue. A-Cos Leasing Corp. v. Wheless,
C.A. Tex. 1970, 422 F.2d 522.

Effective October 1, 1973, a new procedure is mandated by the United States Supreme Court for the District Courts. The mere filing of the petition acts as an automatic stay of all proceedings including mortgage foreclosure proceedings and sales. (Rule 601 of the Bankruptcy Rules.)

On the filing of a voluntary petition pursuant to Rule 10-104 (the present situation) the District Court shall enter an order approving the petition if satisfied it complies with the requirements of Chapter X of the Act and has been filed in good faith. If the Court is not satisfied, the Court shall enter an order permitting the petition to be amended or dismissing the case. The Court may nevertheless hold a hearing on such notices as it may direct on the issue of good faith. Rule 10-113(c).

Rule 10-601 promulgates the concept of an automatic stay and further provides that the stay shall continue until the case is closed, dismissed or converted or until the filing of a complaint seeking relief from the stay provided by this Rule. If a complaint is filed seeking the vacating of the automatic stay, there must be a trial. Rule 10-601(c).

The Rules permit an ex-parte application for the granting of said relief from a stay after a complaint is filed where it

appears from the specific facts shown by an affidavit or a verified complaint that immediate and irreparable injury, loss or damage will result to the plaintiff before the adverse party or attorneys can be heard in opposition and the plaintiff's attorneys certify to the Court in writing efforts if any which have been made to give the notice and reasons supporting the claim. that notice should not be required. Rule 10-601(d).

However, the party obtaining said ex-parte relief must give written or oral notice to the debtor of the vacating of the stay and subsequently on two days' notice to the party who obtained the relief from the stay, the adverse party may appear and move for its reinstatement and the Court shall then proceed to hear and determine on such motion as expeditiously as the ends of justice require. Rule 10-601(d).

None of these procedures were followed by Judge Gagliardi. The debtor-appellant was denied due process under the Rules of this Court and Judge Gagliardi's order was not only improper but void and illegal.

CONCLUSION

THE ORDER OF OCTOBER 20, 1976, WAS IMPROPER.
THIS COURT MUST VACATE SAID ORDER AND DIRECT
THE DISTRICT COURT TO ISSUE A STAY PURSUANT
TO CHAPTER X-113 OF THE ACT.

Dated: Mineola, New York
December 14, 1976

Respectfully submitted,

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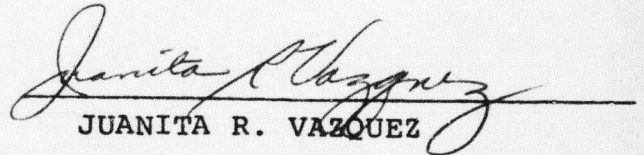
STATE OF NEW YORK)
 SS.:
COUNTY OF NASSAU)

JUANITA R. VAZQUEZ being duly sworn, deposes and says:

That deponent is not a party to the action, is over the age of 18 years and resides at Sea Cliff, New York.

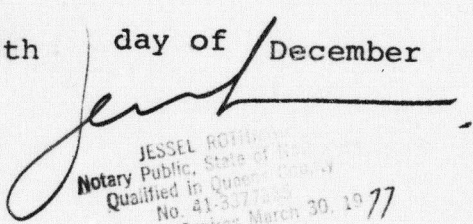
That on the 14th day of December , 1976 , deponent served the within Debtor-Appellant's Brief upon Shea, Gould, Climenko, Kramer & Casey attorney(s) for ~~the~~ Amfac Mortgage Corp. in this action, at 330 Madison Avenue, New York, New York 10017

the address designated by said attorney(s) for that purpose by depositing a true copy of same enclosed in a postpaid properly addressed wrapper, in a post office - official depository under the exclusive care and custody of the United States post office department within New York State.


JUANITA R. VAZQUEZ

Sworn to before me this

14th day of December , 1976


JESSEL ROTHMAN
Notary Public, State of New York
Qualified in Queens County
No. 41-33773-3
Commission Expires March 30, 1977